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February 16, 2007

Commissioner Deborah Taylor Tate
Federal Chair, Federal-State Joint Board on Universal Service
Federal Communications Commission
445 Twelfth St., SW
Washington, DC 20554

Commissioner Ray Baum
State Chair, Federal-State Joint Board on Universal Service
Oregon Public Utility Commission
550 Capitol St., SE, Suite 215
Salem, OR 97308

RE: High Cost Universal Service Support, WC Docket No. 05-337
Federal-State Joint Board on Universal Service, CC Docket No. 96-45

Dear Commissioner Tate and Commissioner Baum:

Consumers in many rural areas rely on high-cost universal service support that carriers use to make available affordable telecommunications services, such as wireless services. Since the entry of competitive eligible telecommunications carriers ("CETCs") into the universal service market, rural areas have greatly benefited from the deployment of basic and advanced wireless universal services. The pro-competitive vision of the 1996 Act has become a reality in many rural areas, but there is more work to be done. As universal service reform measures are considered, such as imposing reasonable limitations on the growth of the universal service fund, they must be accomplished without compromising the pro-consumer principle of competitive neutrality. At the same time, universal service must continue to evolve to promote the development of new broadband networks and advanced services.

Alltel submits a set of concrete proposals to advance these goals. We propose the immediate adoption of a new "pilot" program of "reverse auctions" focused on promoting broadband service for consumers in the most underserved, high-cost areas. Pending

development of a broader transformation of the system in the longer term, we also recommend certain transitional reforms to the existing high-cost support system that can be implemented immediately, designed to (1) target funding more effectively to high cost areas; (2) impose reasonable limits on fund growth; and (3) ensure greater accountability for the use of funds.

To date the explicit universal service funding system has successfully brought consumers in rural America the benefits of access to robust wireless and wireline network infrastructure. Our nation's competitively-neutral universal service program spurs both wireless and wireline companies to expand their networks and introduce new services for consumers and businesses in rural areas.

At the same time, in rural areas as well as in the rest of the country, technological change and increasing competition are transforming consumers' telecommunications needs. Consumers increasingly demand higher-bandwidth services: across the country, purchases of broadband lines increased by 52% from 2005 to 2006, according to recent FCC reports, including an increase from fewer than 400,000 wireless broadband lines in 2005 to over 11 million in 2006. Use of traditional voice-grade wireline telephone lines declined by 3.2% over the same time period. Consumers also increasingly require mobility: mobile wireless service has grown by 50% during the three years ending in December 2005, and consumers now use more wireless than wireline lines. Rural consumers have the same interests in obtaining access to high-speed technologies and mobile services, and are demonstrating changes in demand that parallel those of consumers across the country. But due to the relatively high costs of deploying wireline and wireless networks in many rural areas, these services are being deployed less rapidly in rural areas than elsewhere.

The existing universal service system is not well adapted to this changing environment, and a consensus is emerging that the high-cost support rules need reform. The existing system is designed to support traditional voice-grade wireline services – for which demand is shrinking – and does not target funds effectively to promote development of advanced networks in the highest-cost areas. As a result, high-cost fund amounts per-line are growing in many areas, without efficiently advancing the goals of universal service.

The specific and concrete measures we propose – building on proposals offered by Joint Board member Billy Jack Gregg and a range of industry parties – will not only maintain the availability of existing services in the highest-cost areas, but also will target funding to promote new broadband services. They will establish greater accountability on the use of support funds and will set reasonable limits to the growth of the fund. Critically, these proposed measures also remain true to the Commission's core goal and statutory mandate of maintaining a level playing field for facilities-based, intermodal competition to serve rural consumers.

These policy changes will affect CETCs as much as ILECs. Alltel is not offering these proposals in an intent to benefit or harm any category of providers, but because they will promote the interests of consumers and advance the public interest.

We look forward to working with you on these important matters.

Respectfully submitted,

Gene DeJordy
Steve R. Mowery
Mark Rubin

cc: Joint Board members and staff

ALLTEL UNIVERSAL SERVICE REFORM PROPOSALS

- ***"Pilot" reverse auction system focused on broadband:***
  Use reverse auctions to allocate funds (starting at about $25 million) to bidders that commit to deploy basic and advanced services, including broadband services (*e.g.*, 400 Mbps) in selected unserved and underserved markets.

  – Bidders would offer the lowest amount of funding needed to deploy to specified proportions of the population in the Zip code within given benchmark dates.

  – All ETCs – not just the auction winner – could receive comparable per-line funding if they make the same service commitment.

- ***Reforms to the existing funding system:***

  – ***To limit fund growth:***
  Allow per-line support in each study area to grow by no more than the inflation rate.

  – ***To target funds more effectively:***
  Disburse high-cost funding to geographically disaggregated areas, whether served by "non-rural" carriers or large "rural" ILEC holding companies, as well as CETCs:

    > For purposes of determining funding amounts, consolidate all "study areas" served by a single ILEC holding company in each state into a single study area.

    > Apply the "non-rural" funding rules to such study areas if they have more than 50,000 lines.

    > Revise the "high cost model" forward-looking support mechanism for "non-rural" carriers (including the consolidated study areas of ILEC holding companies formerly deemed "rural") to provide support in the highest-cost wire centers nationwide, not just in 10 states.

    > Require all rural ILEC study areas to be disaggregated for purposes of targeting support to the highest-cost portions of such study areas.

  – ***To ensure accountability:***
  Broaden the FCC's 2005 accountability and reporting requirements and apply them to all ETCs, including ILECs as well as FCC-designated CETCs.

    > Require all ETCs (ILECs as well as CETCs) to document that they are using their funds to maintain and expand service availability for consumers in high-cost areas.

    > Make USAC, rather than NECA (an RLEC-dominated advocacy group), responsible for collecting and processing cost data and determining support amounts.

- ***To protect competitive and technological neutrality:***
  Retain the rule that all ETCs receive the same amount of support per line served.

ALLTEL UNIVERSAL SERVICE REFORM PROPOSALS

I. "Pilot" Reverse Auctions Focused on Broadband Deployment

Ultimately, reverse auctions could be used to allocate ***all*** universal service support. However, complicated and important questions arise in connection with auctions for ***existing*** supported services in a competitively neutral manner, especially where existing ETCs are already serving customers. 1/ Alltel believes that it may be possible to resolve these problems, and that the Commission should continue its work toward developing reverse auctions to set support levels in a competitively neutral manner across the country.

Pending resolution of these broader auction implementation questions, however, Alltel suggests that reverse auctions could be implemented immediately in a manner that would ***target funds to promote broadband deployment*** in unserved or underserved rural areas. Based on the FCC's most recent report on high-speed services, there are approximately 200 Zip code areas in the country where no high-speed, broadband, or advanced services of any kind are being provided, 2/ and presumably many more Zip code areas are underserved. 3/

Alltel proposes an initial "pilot" reverse auction targeted to bring high-speed services to some selection of these unserved or underserved Zip code areas. 4/ In these areas, any ETC (existing or those to be designated in the future) could submit a bid for the minimum amount of universal service support funds ***per line*** that it would need to make available substantial broadband service, as well as the basic services and functionalities supported by the pre-existing high-cost program, to a minimum percentage of households in the Zip code area within a specified period of time. (In areas where an ETC can satisfy this standard without additional support funding beyond that already available under the existing high-cost program, the winning bid might be zero.)

For example, under a hypothetical set of numbers – which could be adjusted as desired – a bidder could be required to commit to deploy facilities enabling it to provide substantial broadband service, as well as pre-existing supported services, on a timely basis to areas comprising **[50%]** of the customers in the Zip code area within **[3]** years of the beginning of the

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1/ *See* Appendix A: "Summary of the State of Hawaii's Use of Auctions to Provide Telecommunications Service in Rural Areas."

2/ *See High-Speed Services for Internet Access: Status as of Dec. 31, 2006* (FCC Wireline Comp. Bur., Industry Anal. & Tech. Div., rel. Jan. 31, 2007). Table 15: "Percentage of Zip Codes with High-Speed Lines in Service" (page 21) indicates that, in ***0.7 percent*** of the nation's 30,000 geographic Zip codes in the country, no "high-speed services" (with at least 200 kbps in at least one direction) are being provided by any provider. The majority of the Zip codes with no broadband service appear to be in areas with relatively low population densities. (*See* Table 18: "High-Speed Subscribership Ranked by Population Density," page 25).

3/ No ADSL or cable modem service is being provided in 12.1% of the nation's Zip codes. *See id.* Table 16: Percentage of Zip Codes with High-Speed Lines in Service by Technology as of June 30, 2006," page 22.

4/ The Zip code areas to be included in this initial auction should be selected by the FCC in a manner that targets at a reasonable level (*e.g.*, $25 million) the overall funds to be disbursed, so as to avoid undue increases in the size of the fund.

six-year auction term, and **[85%]** of the customers in the Zip code area within **[5]** years. 5/ For purposes of this initial pilot auction program only, "broadband" could be included within the definition of "supported services" under Section 254(c) of the Act (although the list of "supported services" would not change with respect to support funds disbursed under the preexisting program). 6/ "Broadband" could be defined as any service used for transmission of information of a user's choosing at a transmission speed of at least 400 kbps in at least 1 direction, regardless of the transmission medium or technology employed. 7/ This definition is higher than the FCC's existing definition, but at a level that reasonably could be met by service providers using a variety of network technologies. An ETC participating in this program would have to file annual reports demonstrating its satisfying the commitments to be capable of serving the specified consumers in the area.

As part of this proposed auction structure, each ETC participating in this program would receive per-line funding only to the extent that it provides the supported service – in this case, both broadband service and the services included in the preexisting definition of universal service – to a customer line. This would provide participating ETCs an even more significant incentive to building out facilities and aggressively promoting broadband subscribership. If the ETC deploys facilities that barely satisfy the applicable requirements, but offers minimal quality service or excessive pricing, so that consumers decline to sign up for its service, the ETC would not receive much funding.

5/ For this purpose, the term "substantial service" could be defined as specified in § 24.203(d) of the FCC's rules, and "timely basis" would be as defined in § 54.202(a)(1)(i)(A) of the rules. The suggested 1/3 and 2/3 service benchmarks are drawn from, but are more aggressive than, the build-out requirements for certain wireless licensees (30 MHz broadband PCS pursuant to § 24.203(a) of the FCC's rules). *See also Facilitating the Provision of Spectrum-Based Services to Rural Areas*, Report and Order and Further Notice of Proposed Rulemaking, 19 FCC Rcd 19078, 19123 ¶ 79 (rel. Sept. 27, 2004) (a wireless carrier would meet a safe harbor for "substantial service" in a rural area if it provides coverage to at least 75% of the geographic area of at least 20% of the counties in the service area that have a population density of 100 or fewer persons per square mile).

6/ The Joint Board and the FCC have broad authority to determine whether to deem such broadband services as a "supported service" under Section 254(c) for a subset of funds under the universal service program. First, the statute itself contemplates that the definition of supported services would be "evolving," that the Joint Board should "recommend… modifications in the definition of the services that area supported," and that the definition should "tak[e] into account advances in telecommunications and information service technologies." *Id.* Whether such services "have been subscribed to by a substantial majority of residential customers" is one of several criteria that may be considered, but is not dispositive. Second, it is clear that different sub-parts of the fund may be used to support different supported services and functionalities; for example, there are separate funds for "local switching support" and "high-cost loop" support. Creation of a new fund targeted to support broadband would be consistent with this scheme. Third, reviewing courts have confirmed the Commission's broad authority to construe Section 254(c), consistent with the deferential *Chevron* standard, so as to advance the public interest. *Texas Office of Pub. Util. Counsel v. FCC*, 181 F.3d 393, 442-43 (5th Cir. 1999). Finally, deeming broadband as a "supported service" for purposes of this pilot reverse auction program would not necessarily require ubiquitous provision of this service by ETCs that do not participate in this program (at least, not right away). If needed, the Commission could exercise its forbearance authority to reach this result.

7/ Source: H.R. 5252, "Communications Opportunity, Promotion, and Enhancement Act of 1996, §254A(e)(1) (Broadband for Unserved Areas Program) (introduced by Sens. Stevens and Inouye and passed by the Senate Commerce Committee on June 28, 2006).

A balance must be struck between ensuring competitive neutrality after the auction closes and providing incentives for auction participants to submit low bids. If only one bidder may receive support post-auction, that would violate competitive neutrality and deprive consumers of competitive options once the auction concludes. On the other hand, incentives for auction participants to submit low bids in this context could be strengthened if auction winners receive some benefits that they would not obtain if they had offered higher bids. For purposes of this pilot broadband auction process, Alltel proposes that the participant offering the lowest bid would receive the full bid amount of per-line support for each broadband line it provides during the duration of the service term (*e.g.*, five years). All other ETCs that commit to meeting the same broadband build-out requirements would ***also*** receive support, but at a slightly lower per-line rate than the winning bidder (*i.e.*, 90 percent of any amounts disbursed over and above the amounts already available under the preexisting high-cost funding programs). This would give participants incentives to offer low bids, but would maximize the number of potential ETCs that could utilize support under this program to provide broadband service to customers in the rural Zip code service area.

Finally, Alltel recommends that the bidding process for the initial "pilot" reverse auction be conducted in a manner similar to that used for spectrum auctions: a multiple round, combinatorial system, in which participants can bid for any number of Zip code areas. The "reserve bid" in each Zip code area would be set based on the current level of high-cost support per line disbursed to ETCs in the area, for example by establishing a maximum bid amount so as not to increase the total per-line support by more than 50% or 100% in any area where high-cost funds are already being disbursed to one or more ETCs. If no ETC submits a bid below this reserve amount for any Zip code area included in this auction, then no additional funds would be disbursed as part of this initial "pilot" auction. This structure also would avoid providing duplicative support (recognizing that the existing support system provides funding for broadband loops and comparable wireless infrastructure), since providers would offer bids only for the additional, incremental support needed to achieve the required deployment targets.

This proposed auction "pilot" has a number of advantages over other plans that have been proposed. First, it would encourage participating carriers to deploy advanced services, such as broadband service, more ubiquitously, because it focuses the funding on such services in unserved and underserved rural areas. 8/ None of the other plans under discussion would offer this benefit. Second, this plan is technology neutral – any service provider, no matter what technology it uses (wireline, wireless, cable-modem, etc.) would qualify to participate in Alltel's proposed program. By contrast, many of the other auctions plans that have been discussed would violate the statutory requirement of competitive and technological neutrality. For example, while the Verizon plan includes some constructive ideas, 9/ the structure of its auctions proposal – with a wireless CETC auction first, followed by a wireline auction – is highly problematic. This approach, not dissimilar from the "discussion paper" attached to the Joint

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8/ In this respect, this proposal is consistent with the proposed measures to target the pre-existing funding mechanisms more narrowly, as discussed in section II.B. below.

9/ *Ex Parte* Letter from Kathleen Grillo, Verizon, to Deborah Taylor Tate and Ray Baum, CC Docket No. 96-45, WC Docket No. 05-337 (filed Feb. 9, 2007) ("*Verizon Ex Parte*").

Board's 2006 public notice, 10/ most likely would result in substantial reductions in fund levels to one wireless CETC, while eliminating funding for all others, while maintaining existing funding for wireline ETCs (ILECs), at least for the short- to medium-term. This would unreasonably discriminate against wireless companies, in violation of the Act and well established law, and to the detriment of consumers and intermodal, facilities-based competition. It also would thwart efficient investment in rural areas. Such a discriminatory system would be particularly anomalous given that the wireless industry now bears a greater burden of paying for universal service support than any other category in the telecommunications industry. 11/

The purpose of any universal service auction – particularly (but not only) an auction focused on bringing new broadband infrastructure to underserved areas – should not be to select a single "winner," or even a limited number of winners, but rather to determine an efficient level of support that is the minimum necessary to ensure the desired level of service in each geographic area. In other words, rather than trying to use competitive bidding as a substitute for actual competition, an auction-based funding system could complement the competitive market's incentives for carriers to efficiently invest in rural markets and to provide high-quality service to rural consumers. 12/ This would avoid distorting the marketplace after the auction is concluded and ensure that consumers receive the benefits of both universal service and competition.

II. Transitional Reforms to the Existing Universal Service System

In addition to a new pilot reverse auction program, Alltel proposes the following reforms to the existing high-cost funding mechanisms that could be implemented immediately. These measures would benefit consumers right away, and would lay the groundwork for a more fundamental transformation of the high-cost program over the next few years. Specific rules drafted to implement these measures are included in Appendix B ("Specific Rule Changes to Implement Alltel Transitional Reform Proposals").

A. Allow Per-Line Support In Each Study Area To Grow By No More Than The Inflation Rate

Per-line support – the amount of support disbursed *per line served* in each study area, as distinct from the *total* amount of support – is growing considerably in many rural ILEC study areas. Line counts for ILECs across the country, including rural ILECs, are declining, as

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10/ *Federal-State Joint Board Seeks Comment on the Merits of Using Auctions to Determine High-Cost Universal Service Support*, Public Notice, WC Docket No. 05-337; CC Docket No. 96-45, FCC 06J-1 21 FCC Rcd 9262 (2006), Attachment ("Discussion Proposal").

11/ *See* Notice of *Ex Parte* Presentation of Alltel Corp., CC Docket No. 96-45 at 9, 12 (filed Jan. 12, 2007) ("*Alltel Ex Parte*").

12/ The failed experience with a universal service auction experiment in the mid-1990s in Hawaii, in which an ill-conceived auction was instituted in an effort to establish a new sole provider in a rural portion of the big island of Hawaii, rather than introducing competition, demonstrates the grave difficulties of trying to implement such an approach. Appendix A to this paper provides a summary of the problematic Hawaii auctions plan.

customers shift from traditional phone service to DSL, other broadband service, or wireless. Under the existing "rate of return" system, if "revenue requirements" (embedded costs) remain constant but line counts decline, the per-line support amount will grow. (The numerator of the fraction remains constant but the denominator gets smaller.) This growth in per-line support due to reduced line counts and service substitution may occur regardless of whether consumers are shifting their service from traditional ILEC lines to alternative services provided by the ILECs themselves or provided by alternative carriers that may, or may not, be designated as competitive ETCs. However, the effect may be more significant in the presence of competitive ETCs, which are obligated to target services to rural consumers.

A number of parties have proposed to adopt limitations on the growth of per-line support in each study area. 13/ Under the version of this proposal fleshed out below, the amount of support per-line in each study area would be adjusted upward each year to account for inflation, 14/ but could not increase by more than this amount over the amount disbursed during the preceding year. This would enable each carrier's total amount of support funding to grow as it manages to serve additional customers, but not otherwise. For the time being this would retain the rural ILECs' existing basis for funding, but would prevent the amount of funding per line from growing disproportionately due to service-substitution.

This proposal would strengthen incentive for all ETCs – ILECs and competitive ETCs alike – to not only build and improve their networks, but also to promote their services to consumers and make them as appealing as possible – *i.e.*, to compete more vigorously. This will have the effect of increasing not only a carrier's own subscriber base, but also the total telecommunications subscribership level in the service territory. Successful competitors would increase their support (as well as their consumer revenues) by obtaining additional customer lines. At the same time, no carrier would experience dramatic revenue shifts as a result of this proposal. This proposal also would be consistent with the FCC's intent in adopting rule 54.307 (the competitive ETC support rule): that as competitive ETCs "capture the subscriber lines" of an ILEC, the competitive ETC rather than the ILEC would receive the support for those lines. 15/

This rule change would be generally consistent with the 2000 recommendation of the Federal-State Joint Board on Universal Service's Rural Task Force proposal to freeze high-cost

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13/ *See, e.g., Alltel Ex Parte* at 37-38; Public Notice, *Federal-State Joint Board on Universal Service Seeks Comment on Proposals to Modify the Commission's Rules Relating to High-Cost Universal Service Support*, 20 FCC Rcd 14267 at Appendix B (rel. Aug. 17, 2005) ("*Billy Jack Gregg Stage One Proposals*"); *Ex Parte* Communication of CTIA – The Wireless Association, CC Docket No. 96-45, WC Docket No. 05-337 at 2 (filed Jan. 24, 2007) ("*CTIA Ex Parte*"); Comments of CTIA – The Wireless Association, CC Docket No. 06-45 (filed Oct. 15, 2004) ("*CTIA Comments*"); Comments of General Communication Inc., WC Docket No. 05-337 at 17-18 (filed Oct. 10, 2006) ("*GCI Comments*"); Comments of the National Cable & Telecommunications Association, WC Docket No. 05-337 at 2-4 (filed Oct. 10, 2006). For a slightly different version of funding caps, *see Verizon Ex Parte* at 4-5.

14/ Alltel would support the use of an inflation factor based on the "GDP-CPI," consistent with the proposal in H.R. 5072, introduced by Rep. Terry and Rep. Boucher on March 30, 2006.

15/ *Federal-State Joint Board on Universal Service*, First Report and Order, 12 FCC Rcd 8776, 8786, ¶ 15 (1997); *GCI Comments* at 17-18.

support upon competitive entry. The key difference is that, since 2000, competitive ETCs already have been certified in rural study areas that include the majority of rural ILEC subscriber lines. Line substitution is not being caused solely due to entry by competitive ETCs; for example, many customers are retaining their ILEC primary lines but dropping their second lines and instead opting for ILECs' (or other service providers') broadband access. Accordingly, the limitation on per-line support growth under this proposal would not be triggered by designation of a competitive ETC.

This proposal also differs from some other proposals regarding fund growth caps that have been under discussion. The plan recently offered by Verizon would impose separate caps on wireless vs. wireline funding growth. 16/ As a result, disparities would grow between the per-line funding disbursed to these categories of categories. Given the more rapid growth of wireless subscribership, the per-line funding to wireless carriers most likely would drop, while per-line funding to ILECs would likely increase. This would violate competitive neutrality by strengthening the ILECs' ability to compete vis-à-vis wireless ETCs. Another version of fund growth caps would impose an inflation-based limit on the *total* growth of support within each study area or service area. Under this approach, the per-line amount of support would remain the same for all ETCs serving the study area, but the amount of support would decline more rapidly because all ETCs would receive proportionally less support as the total number of ETC lines grow. This approach, endorsed by the Joint Board and by many carriers in the past (including Alltel and its predecessor, Western Wireless) would be effective at limiting the fund, but also would have more dramatic impacts on individual small carriers than the plan discussed above.

B. Target Funding To The Highest-Cost Areas

The existing high-cost funding rules suffer three related problems that reduce the system's effectiveness and efficiency in achieving the goal of promoting universal service for consumers in high-cost areas. First, large ILEC holding companies with multiple "rural" "study areas" may receive excessive funds purportedly based on embedded costs. At the same time, so-called "non-rural" ILECs serving similar geographic areas receive little or no support (as do competitive ETCs in those areas) under the forward-looking model based support mechanism. And support is distributed on an averaged basis to most "rural" study areas rather than in a manner that targets funds more narrowly to high-cost portions of those study areas. As a result of this erratic and inconsistent funding system, consumers in many high-cost areas are deprived of access to the supported services.

Specific rule changes to address these problems could reduce the overall size of the fund while more effectively promoting universal service, and could be implemented immediately pending development of more broad-scale rule changes. In particular, we propose to disburse high-cost funding in a more targeted manner that does not vary based on whether an area is served by "non-rural" ILECs, large "rural" ILEC holding companies, or CETCs, as follows:

16/ *Verizon Ex Parte* at 4-5.

– For purposes of determining funding amounts, consolidate all "study areas" served by a single ILEC holding company in each state into a single "study area."

– Apply the "non-rural" funding rules to such "study areas" if they have more than 50,000 lines.

– Revise the High Cost Model ("HCM") forward-looking support mechanism for "non-rural" carriers, including the consolidated study areas of ILEC holding companies formerly deemed "rural," to provide support in the highest-cost wire centers nationwide, not just in 10 states.

– Require all rural ILEC study areas to be disaggregated for purposes of targeting support to the highest-cost portions of such study areas.

These changes may reduce the overall amount of support to ILECs and CETCs alike, but would target such support more effectively to the highest-cost areas, so that – for example – less support could be disbursed in town centers and more support in outlying areas. 17/

1. Consolidation of Study Areas

First, some ILEC holding companies maintain numerous separate "study areas" within each state, corresponding to previously separate rural ILEC companies that have been consolidated or "rolled up" by these large holding companies. Even though the ILEC holding companies in these states can achieve operating efficiencies of scale (for example, by purchasing equipment in bulk and efficiently deploying maintenance personnel over a larger area), the existing embedded cost-based support mechanisms continue to calculate support funds for these "study areas" as if they were still separate companies. This problem can be resolved – reducing the total size of the fund without having any negative impact on universal service – by consolidating all "study areas" served by a single ILEC holding company in each state into a single "study area" for purposes of calculating universal service funding amounts. Moreover, following such study area consolidation, any ILEC holding company that has over 50,000 lines in a given state should be entitled to the non-rural support funds (HCM and IAS), rather than the funds intended for the smallest ILECs in the state. Any reduction in per-line support would apply to competitive ETCs as well as ILECs affected by these rule changes. This proposal has been endorsed by a wide range of parties. 18/

Alltel's preliminary analysis indicates that this proposal would affect approximately 15.8 million lines in about 150 "study areas," including 13.9 million ILEC lines and 1.9 million CETC lines. At present about $535.5 million annually is disbursed to these areas, including about $408.6 million to ILECs and $127.0 million to CETCs. (The totals are affected by rounding; and some of the affected carriers' loss of support under this proposal would be offset

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17/ *See Ex Parte Filing of Embarq Corp.*, WC Docket No. 05-337 (filed Feb. 2, 2007) ("*Embarq Ex Parte*"). This could be implemented only in "rural" ILEC study areas, or in "rural" study areas as well as "non-rural" wire centers or other geographic units.

18/ *See, e.g., Billy Jack Gregg Stage One Proposals*, which proposes a 100,000 threshold.

by increased in HCM support as described below.) 19/ Alltel cannot predict exactly how much this proposal would reduce high-cost support to these relatively large carriers, but if only 30% of these funds were reduced, the overall high-cost fund would save over $150 million per year -- with virtually no serious impact on the affected carriers' ability to provide universal service.

2. Reform of the High Cost Model Fund

Consumers in rural areas in many states have no access to universal service high-cost funding, even though such funding is needed to assure that they receive the supported services. To address this problem in tandem with the proposal to consolidate rural ILEC study areas and move many of them into the "non-rural" system, the forward-looking High Cost Model ("HCM") mechanism used in such "non-rural" areas should be modified to disburse funds to the highest cost geographic areas in all states (not just ten). At present, the HCM uses averaging assumptions that result in distributing support in only ten states. This means that no HCM support is disbursed in any of the other states served by non-rural ILECs, even in the highest-cost areas – depriving consumers in these regions of the explicit federal support funding needed to promote universal service to them. The existing mechanism also relies improperly on implicit averaging by large "non-rural" ILECs.

Alltel supports reform to the existing HCM rules to distribute a modest amount of additional support to carriers serving these high-cost areas, consistent with that proposed by Rep. Terry and Rep. Boucher in § 254(e)(3)(A) of H.R. 5072 (introduced March 30, 2006). It is difficult to calculate the impact of this proposal. A possible way to structure it would be, as, to assure funding to any wire center – whether "rural" or "non-rural" – in which the forward-looking cost of service exceeds 3.75 times the national average, as specified in the Terry/Boucher bill), although the specific numbers could be adjusted as necessary. The additional support to these areas could be computed in a manner similar to the existing HCM, which disburses 76% of the difference between the forward-looking cost and a national cost benchmark (or using a modified percentage or benchmark level). These figures should be adjusted to ensure that the net effect of this and the study area consolidation proposal discussed above would reduce the overall size of the fund by the desired amount, while more accurately targeting the remaining funding.

3. Rural Study Area Disaggregation

Rural ILECs were given an "option" in 2001 to "disaggregate" support so as to focus more support in the higher-cost portions of their study areas and less support on the lower-cost portions. Almost none of the rural ILECs have exercised this option. To the extent a system of disaggregation targets funding to more effectively promote universal service, such a system should be required in all rural study areas, subject to a consistent methodology overseen by state or federal regulators, and not just where ILECs find it advantageous to opt into it. This proposal

19/ In addition, in the event of unusual hardships that these changes might cause a particular study area, an ILEC or CETCs in that area could request a waiver to enable additional per-line funding to be disbursed to all ETCs serving that area.

also has widespread support, 20/ and would not have any immediate net impact on the size of the fund or on the amounts of support distributed to particular categories of ETCs.

C. Heightened Accountability For Use of Funding

Alltel strongly supports rigorous controls to ensure that funds are actually being used in a manner that furthers the goals of the universal service fund. In 2005 the FCC adopted stringent rules requiring FCC-designated ETCs to submit annual reports regarding their five-year service quality improvement plans, including detailed information regarding how much universal service support was received, and how it was used to improve signal quality, coverage, or capacity, and an explanation regarding any network improvement targets that have not been fulfilled. Many states have imposed comparable requirements on competitive ETCs. These rules made progress toward ensuring that ETCs are accountable for the funds that they receive and spend – but could go further to address any issues – actual or perceived – of accountability for the use of universal service funds.

The FCC's current ETC reporting rules apply only to carriers that received designation from the FCC – in nearly all cases, competitive wireless ETCs. Many state commissions adopted similar rules for CETCs. By contrast, ILECs are under no similar obligation to report on the manner in which they use the support they receive to improve their networks and benefit consumers. The reports submitted by ILECs are much *less* rigorous than those that CETCs are currently required to submit. Alltel proposes revising the FCC's rules to apply to all ETCs, including ILECs as well as CETCs, whether designated by the FCC or by a state commission. This would provide much greater assurance of the integrity of the program. In addition, Alltel proposes a rule that requires all carriers to demonstrate that they are using all high-cost support received in a manner that inures to the benefit of the consumers in the relevant geographic area.

Finally, Alltel proposes vesting responsibility for collecting and processing rate-of-return ILECs' cost and revenue data with the Universal Service Administrative Co. (USAC), instead of the National Exchange Carriers Association (NECA). NECA is a trade group consisting exclusively of ILECs that participates actively in FCC proceedings and elsewhere as a policy advocate on behalf of the rural ILEC community. Pursuant to Part 69 of the FCC's rules NECA administers access charge tariffs on behalf of many of the rural ILECs – an efficient way to organize this cumbersome process. However, NECA also is the only entity that processes and reviews the data that determine the amounts of HCL, LSS, and ICLS universal service funding disbursed in rural ILEC study areas. Neither the FCC nor state commissions review these data. Vesting this responsibility with an advocacy organization like NECA is comparable with placing the fox in charge of the chicken coop, and creates a serious risk that some rural ILECs could take advantage of the lax oversight now in place. 21/

20/ *See, e.g., Embarq Ex Parte; CTIA Ex Parte* at 7.

21/ *See* "Fees Paid by All Phone Customers Help Rural Phone Firms Prosper," USA Today, Nov. 17, 2004 (available at http://www.usatoday.com/money/industries/telecom/2004-11-15-rural-phone-fees_x.htm) ("But critics say the system is laced with waste and inefficiency. They point to some rural phone companies'

Alltel respectfully submits that, while NECA may be an appropriate organization to administer access tariffs, it is inappropriate for an advocacy group representing a single industry sector to administer an important component of the high-cost universal service program. This responsibility should be transferred to USAC. In the alternative, as recommended by the Joint Board in 1996 and adopted in a Report and Order in 1997, 22/ NECA should be reformed so that its Board of Directors, like USAC's, be representative of the industry as a whole rather than just one industry segment. Under this approach, NECA, like USAC, would be strictly prohibited from engaging in any public policy advocacy before the FCC or elsewhere. 23/

III. Competitive and Technological Neutrality

Alltel takes the opportunity to briefly address some of the other proposals under consideration by the Joint Board and the Commission. The Joint Board and the Commission should not consider a proposal that would depart from competitive neutrality by granting competitive ETCs support based on their "actual costs" if less than ILEC "embedded costs," but would cap CETC support at the per-line amount disbursed to ILECs. 24/ This proposal would not impose any cap on ILEC support, even if competing wireless carriers can provide service more efficiently at lower costs. This patently unfair proposal would violate competitive neutrality and harm consumers. It also would be virtually impossible to implement at least in the short- to medium-term.

First, it is beyond dispute that any system that would assure funds to ILECs while denying them to competitors would grant these companies "protection from competition, the very antithesis of the Act." 25/ Since 1996, the Commission and reviewing courts have held that fund portability – *i.e.*, granting competitors per-line funding that is the same as to incumbents – is mandated by the Act. 26/ This so-called "actual costs" proposal (*i.e.*, a CETC would receive

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high overhead, sumptuous earnings, rich dividends and, at least in one case, fraud. Oversight has been lax…."). *See also* "Rural Phone Service Fund Under Siege," USA Today, Jan. 20, 2005 (available at http://www.usatoday.com/money/industries/telecom/2005-01-19-rural-fund-usat_x.htm).

22/ *See* Report and Order and Second Order on Reconsideration, CC Docket Nos. 96-45, 97-21, 12 FCC Rcd 18400 (rel. Jul. 18, 1997).

23/ *Cf.* 47 C.F.R. § 54.702(d) ("The Administrator may advocate positions before the Commission and its staff only on administrative matters relating to the universal service support mechanisms.").

24/ *See, e.g., Billy Jack Gregg Stage One Proposals.*

25/ *Alenco Communications, Inc. v. FCC*, 201 F.3d 608, 622 (5th Cir. 2000); *see also id*. at 616 (the universal service program "must treat all market participants equally--for example, subsidies must be portable--so that the market, and not local or federal government regulators, determines who shall compete for and deliver services to customers.")

26/ The Fifth Circuit held in *Alenco* that "portability is not only consistent with [the statutory requirement of] predictability, but also is dictated by the principles of competitive neutrality and the statutory command [of section 254(e)]." 201 F.3d at 622. The Commission has stated that "it is difficult to see how [a non-portable funding mechanism] could be considered competitively neutral" because "a mechanism that offers non-portable support may give ILECs a substantial unfair price advantage in competing for customers." *Western Wireless Corp. Petition for Preemption of Statutes and Rules Regarding the Kansas State Universal Service*

support based upon its costs only if its costs are lower than the ILECs, but if its costs are higher then it would get the portable per-line equivalent to the ILEC support), by design, inevitably would disburse more support to ILECs than to competitors using alternative technologies, and would violate the findings of the *Alenco* court.

Moreover, strict application of the competitive and technological neutrality principle benefits rural consumers. "Commenters who express concern about the principle of competitive neutrality… *present a false choice between competition and universal service*. A principal purpose of section 254 is to create mechanisms that will sustain universal service as competition emerges. We expect that applying the policy of competitive neutrality will promote emerging technologies that, over time, may provide competitive alternatives in rural, insular, and high cost areas and thereby benefit rural consumers." 27/ Auctions initially targeted at supporting a single technology would violate the principle of technological neutrality. Auctions also could be disruptive to existing ETCs that receive funding, and must be structured so as to ensure that competition in the auction bidding process does not have a harmful impact on marketplace competition once the auctions are concluded.

Finally, given the analytical difficulties of calculating "actual costs" for unregulated companies, it would be virtually impossible to implement an "actual costs" approach for wireless carriers in the short- to medium-term. The insurmountable complexities of this proposal are discussed in detail in Appendix C.

Fund Pursuant to Section 253 of the Communications Act of 1934, File No. CWD 98-90, Memorandum Opinion and Order, 15 FCC Rcd 16227, 16232, ¶ 10 (2000). Furthermore, the Commission has specifically considered and rejected arguments that portable support based on ILEC costs gives an unfair advantage to competitors. *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, First Report and Order, 12 FCC Rcd 8776, 8933, ¶ 289 (1997) ("While the CLEC may have costs different from the ILEC, the CLEC must also comply with Section 254(e) . . . . If the CLEC can serve the customer's line at a much lower cost than the incumbent, this may indicate a less than efficient ILEC." (citations omitted)).

27/ *Federal-State Joint Board on Universal Service*, First Report and Order, 12 FCC Rcd 8776, ¶ 50 (1997), *subsequent history omitted* (emphasis added, footnotes omitted).

Appendix A: Summary of the State of Hawaii's Use of Auctions To Provide Telecommunications Service in Rural Areas

In the early 1990s, many residents of the rural Ka'u district of the big island of Hawaii were dissatisfied with the poor quality of service provided by the incumbent local exchange carrier (ILEC), GTE Hawaiian Tel, and by the lack of any service at all in many parts of the district. In response to these concerns, in December 1995, the Public Utilities Commission of the State of Hawaii ("Hawaii PUC") decided to launch a pilot reverse auction to bring in better service to the Ka'u district; it concluded that "proposals to provide telecommunications service in the rural areas of the State shall be submitted to the commission in accordance with the proposal and bid specifications to be established by the commission." 28/ Recognizing that wireless carriers may be best suited to serving rural areas, the Hawaii PUC "welcome[d] proposals from wireless carriers that may be interested in serving the pilot project area." 29/ The Hawaii PUC ultimately received proposals from four carriers, GTE Hawaiian, two competitive local exchange carriers (TelHawaii and GST Hui Keleka'a'ike), and one wireless carrier (VoiceStream). 30/

In the end, Hawaii's bidding process for telecommunications in rural areas was declared invalid by the courts, which concluded, among other things, that Hawaii's auction process was inconsistent with the law because "it allows TelHawaii [the winning bidder] what amounts to an exclusive franchise to serve the Ka'u District, unhindered by competition. This grant of exclusivity is in direct contradiction of §§253 and 254 of the FTA [federal Telecommunications Act]." 31/

On August 2, 1999, Honolulu's leading business weekly, the *Pacific Business News*, described the last chapter of Hawaii's failed bid experiment:

> [O]n the Big Island, rural telecom carrier TelHawaii has announced plans to cease operations, most likely by the end of August if not sooner.
>
> The Company was awarded a contract by the state Public Utilities Commission in 1996 to provide service to the underserved rural Ka'u area.
>
> However, despite spending millions on switching equipment in preparation for offering service, TelHawaii spent a great deal of time

28/ *In the matter of GTE Hawaiian Telephone Company Incorporated*, Order to Show Cause, Docket No. 94-0346, Decision and Order No. 14415, filed December 13, 1995.

29/ *Id.* at p. 19.

30/ *In the matter of GTE Hawaiian Telephone Company Incorporated*, Order to Show Cause, Docket No. 94-0346, Decision and Order No. 14789, filed July 15, 1996. VoiceStream is now part of T-Mobile; at the time, it was a wholly-owned subsidiary of Western Wireless, which has since merged with Alltel in August 2005.

31/ *GTE Haw'n Tel v. Pub. Util. Comm'n*, Findings of Fact, Conclusions of Law and Order, Civil No. 97-4372-10 (Haw. 1st Cir. Ct. Apr. 1, 1999).

fighting off court challenges from incumbent carrier GTE Hawaiian Tel, which TelHawaii was scheduled to replace.

The Ka'u area of the Island of Hawaii is a rural area with relatively few users spread over a large geographic area of Hawaii's largest island. Complaints about inadequate telephone service from residents and businesses in Ka'u (and other rural areas of the State) become a critical issue in the state, resulting in the Hawaii PUC launching an investigation of rural telecommunications service. Following two years of public hearings and contested case proceedings, the Hawaii PUC found that the telephone service provided by the ILEC was inadequate in the rural areas of the state. 32/

At approximately the same time that the Hawaii PUC was conducting its investigation, the Hawaii Legislature passed Act 80, Session Laws of Hawaii (1994) requiring the Hawaii PUC, upon determination that an area was receiving inadequate telecommunications service, to order the carrier providing inadequate service to show cause why the Commission should not replace the carrier with an adequate service provider. Having already ruled that the ILEC's rural telephone service was inadequate just the month previous, the auction process was set in motion.

The Hawaii PUC identified the following issues for addressing inadequate telephone service in rural areas: 33/

1. Whether the Commission should authorize an alternative telecommunications provider for the rural areas of the State.
2. Whether Decision and Order No. 13626, filed on November 2, 1994, in Docket No. 7497 (the investigation of the ILEC's service in the rural areas of the State), obviates the need for this docket.
3. Whether alternative providers can provide the same or better service to customers in the rural areas of the State at a lower or competitive cost.
4. What network interconnection arrangements if any will be necessary between GTE Hawaii Tel and an alternative provider authorized to serve the rural areas of the State?
5. What other types of arrangements, e.g., space on or in the ILEC's poles, conduits, and easements, will be necessary between the ILEC and an alternative provider authorized to serve the rural areas of the State.
6. If there are two or more alternative providers interested in serving a rural area, how should the alternative provider be selected?
   a) Bid process?
   b) Selected by residents?
   c) Selected by the Commission?

A number of features in the auction design were problematic. First, the auction did not contemplate allowing multiple carriers to compete in providing services supported by the

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32/ *In re GTE Haw'n Tel*, Order No. 11886, Docket No. 7497 (Nov. 2, 1994).

33/ *In the matter of GTE Hawaiian Telephone Company Incorporated*, Order to Show Cause, Docket No. 94-0346, Order No. 13763, filed Feb. 10, 1995.

universal service program, or even to compete at all. Rather, the auction was designed to select, in essence, a single provider of telecommunications for the area – a goal that the court found to violate governing law.

Second, the auction was structured to maximize federal fund disbursements and subsidies (prior to the adoption of the so-called "parent trap rule," 47 C.F.R. § 54.305, a service provider serving a smaller service area could obtain greater funding than a larger entity such as GTE Hawaiian Tel). The Hawaii PUC identified access to federal universal service funds as a key factor in selecting a service provider: "It is clear from this evidence that a telecommunications provider that has access to funding from the national universal service fund and for low cost loans should be able to provide the same or better service to customers in the rural areas of this State at a lower cost than GTE Hawaiian Tel." 34/

Third, the auction winner was not to be selected based on clear and impartial standards, but based on multiple vague criteria, which ultimately opened the agency to charges of partiality in selecting a favored provider. The selection of a service provider was not based on the lowest bid (which would have been a clear, principled standard), but on an applicant's purported internal strengths, external strengths, and miscellaneous indicia of fitness and ability, including the degree of support for a particular carrier in the affected area, as explained below: 35/

(1) threshold inquiry-internal strengths:
    organization
    financial backing
    technical facilities
    operations expertise
    management and administrative experience;
(2) secondary inquiry-external strengths:
    proposed rates (lowest bid)
    rate design
    track record
    demonstrated alertness to consumer needs and desires
    consumer preferences
    impact on entitles other than competing applicants
    local ownership control; and
(3) final inquiry-miscellaneous factors:
    first in the field status
    first in the application process
    quality of application
    ongoing regulatory control
    overall general fitness.

34/ *In re GTE Haw'n Tel*, Docket No. 94-0346, Decision and Order No. 14415 (Dec. 13, 1995) at 8-9.

35/ *Id*.

The Hawaii PUC ended up selecting TelHawaii, a CLEC, to serve the Ka'u area without fully explaining how it reached its decision. 36/ Upon motion for reconsideration and clarification filed by the ILEC, the Hawaii PUC clarified that it was not designating TelHawaii as the exclusive provider of basic telephone service for the Ka'u area. 37/ Complicated questions were raised, however, about the auction winner's access to and interconnection with the ILEC's network facilities, and about a transition, if any, from the ILEC to the auction winner as service provider. Thereafter, legal challenges ensued, resulting in the court's decision to invalidate the Hawaii PUC's experiment with auctions.

36/ *In re GTE Haw'n* Tel, Docket No. 94-0346, Decision and Order No. 14789, (Jul. 15, 1996) at 2.

37/ Order No. 14883 (Aug. 15, 1996).

Appendix B – Specific Rule Changes to Implement Alltel Transitional Reform Proposals

1. In Part 36, sections 36.611, 36.612, and 36.613, are revised by deleting every reference to "the National Exchange Carrier Association (NECA)" or "NECA" and inserting, in its place, "the universal service Administrator established under Part 54, Subpart H".

2. In the Appendix to Part 36-Glossary, the definition of "*Study Area*" is revised to read as follows: [The text in **bold** font is in the existing definition; the additional text is underlined.]

Study Area

Study area boundaries shall be frozen as they are on November 15, 1984, subject to study area waivers granted by the Commission since that date; *provided* that for purposes of computing universal service high-cost support funding under subpart F of this Part and Part 54, subparts D, J and K, of this chapter, all such study areas in a state shall be deemed a single study area to the extent that they are served by a single incumbent local exchange carrier or by incumbent local exchange carriers that are "affiliates" of one another as defined in 47 U.S.C. 153(1).

3. Part 54, sections 54.202 and 54.209, are revised by deleting every reference to "under section 214(e)(6)" and inserting, in its place, "under section 214(e)(2) or section 214(e)(6)."

4. Part 54, section 54.209, paragraph (a)(7) is revised to read as follows:

"(7) Certification that the carrier is using all high-cost support received in a manner that inures to the benefit of the consumers in the service area or the relevant disaggregation zone; and".

5. In Part 54, Subpart D ("Universal Service Support For High Cost Areas"), the following new section is added:

§ 54.300 Limitation on Growth of Per-Line Support.

(a) *Limitation*. Notwithstanding any other provision in this chapter, beginning on January 1, [2008], the amount of support funding disbursed per line for each of the categories specified in paragraph (b) of this section to each eligible telecommunications carrier operating in each study area of a rural incumbent local exchange carrier, and/or in each disaggregation zone if such disaggregation zones have been established pursuant to § 54.315 of this subpart, during each year shall not exceed the amount per line of such support that was disbursed to eligible telecommunications carriers during the fourth calendar quarter of the preceding year in such study area and/or disaggregation zone, as adjusted based on the Inflation Factor specified in paragraph (c) of this section.

(b) *Categories of Support*. The limitation on per-line funding growth specified in paragraph (a) of this section shall apply separately to each of the following categories of universal service support funding:

(1) High-Cost Loop Support, including the total of the universal service support mechanisms provided in Part 36, Subpart F of this chapter and in § 54.305 of this subpart;

(2) Local Switching Support, as provided in § 54.301 of this subpart; and

(3) Interstate Common Line Support, as provided in Subpart K of this Part.

(c) *Inflation Factor*. For purposes of paragraph (a) of this section, the Inflation Factor is the annual percentage change in the United States Department of Commerce's Gross Domestic Product—Chained Price Index (GDP-CPI) during the preceding calendar year, but not less than zero.

6. Section 54.309 is revised by inserting the following paragraph (c) and redesignating the existing paragraph (c) as (d):

(c) *Support for the Highest-Cost Wire Centers Served by Non-Rural Carriers*. Beginning January 1, [2008], additional support shall be disbursed to eligible telecommunications carriers in each wire center in which no universal service support is otherwise available pursuant to paragraph (b) of this section or Subpart K of this Part, and in which the forward-looking economic cost (FLEC) per line of providing the supported services, as determined under paragraph (a) of this section, exceeds **[3.75]** times the national average (FLEC) per line. The per-line amount of such support shall be calculated based on **[76]** percent of the amount by which the FLEC per line in such wire center exceeds the national cost benchmark specified in paragraph (a)(3) of this section. Support distributed pursuant to this paragraph shall not be included in the total support available per state calculated pursuant to paragraphs (a)(4) and (b) of this section.

7. Section 54.315 is revised to read as follows. (Insertions are marked in *italic* font; deletions are in ~~strikeout~~ font.)

§ 54.315 Disaggregation and targeting of high-cost support.

(a) *Beginning on January 1, [2008],* ~~On or before May 15, 2002,~~ all rural *study areas* ~~incumbent local exchange carriers and rate-of-return carriers~~ for which high-cost universal service support pursuant to §§ 54.301, 54.303, and/or 54.305 of this subpart, subpart K of this part, and/or part 36 subpart F is available *shall be subject to* ~~must select a~~ disaggregation ~~path~~ as described in paragraph~~s (b), (c), or~~ (d) of this section. ~~In study areas in which a competitive carrier was designated as a competitive eligible telecommunications carrier prior to June 19, 2001, the rural incumbent local exchange carrier or rate-of-return carrier may only disaggregate support pursuant to paragraphs (b), (c), or (d)(1)(iii) of this section. A rural incumbent local exchange carrier or rate-of-return carrier failing to select a disaggregation path as described in paragraphs (b), (c), or (d) of this section by May 15, 2002, will not be permitted to disaggregate and target federal high-cost support unless ordered to do so by a state commission as that term is defined in § 54.5.~~

(b) *[Deleted.]* ~~Path 1: Carriers Not Disaggregating and Targeting High-Cost Support:~~

~~(1) A carrier may certify to the state commission that it will not disaggregate and target high-cost universal service support.~~

~~(2) A carrier's election of this path becomes effective upon certification by the carrier to the state commission.~~

~~(3) This path shall remain in place for such carrier for at least four years from the date of certification to the state commission except as provided in paragraph (b)(4) of this section.~~

~~(4) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by the rural incumbent local exchange carrier or rate-of-return carrier, the disaggregation and targeting of support under paragraphs (c) or (d) of this section.~~

~~(5) A carrier not subject to the jurisdiction of a state, e.g., certain tribally owned carriers, may select Path 1, but must certify to the Federal Communications Commission as described in paragraphs (1) through (4) of this section.~~

(c) *[Deleted.]* ~~Path 2: Carriers Seeking Prior Regulatory Approval for the Disaggregation and Targeting of Support:~~

~~(1) A carrier electing to disaggregate and target support under this paragraph must file a disaggregation and targeting plan with the state commission.~~

~~(2) Under this paragraph a carrier may propose any method of disaggregation and targeting of support consistent with the general requirements detailed in paragraph (e) of this section.~~

~~(3) A disaggregation and targeting plan under this paragraph becomes effective upon approval by the state commission.~~

~~(4) A carrier shall disaggregate and target support under this path for at least four years from the date of approval by the state commission except as provided in paragraph (c)(5) of this section.~~

~~(5) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by the rural incumbent local exchange carrier or rate-of-return carrier, the disaggregation and targeting of support in a different manner.~~

~~(6) A carrier not subject to the jurisdiction of a state, e.g., certain tribally owned carriers, may select Path 2, but must seek approval from the Federal Communications Commission as described in paragraphs (c)(1) through (5) of this section.~~

(d) ~~*Path 3: Self-Certification of the*~~ *Disaggregation and Targeting of Support*:

(1) A carrier designated as an eligible telecommunications carrier in a study area may file a disaggregation and targeting plan for approval by ~~with~~ the state commission. If alternative disaggregation and targeting plans are filed by more than one eligible telecommunications carrier in a study area, the state commission shall select the plan that most effectively aligns zone boundaries and support funding amounts in each zone with cost. ~~along with a statement certifying each of the following:~~

~~(i) It has disaggregated support to the wire center level; or~~
~~(ii) It has disaggregated support into no more than two cost zones per wire center; or~~
~~(iii) That the carrier's disaggregation plan complies with a prior regulatory determination made by the state commission.~~

(2) Any disaggregation plan submitted pursuant to this paragraph must meet the following requirements:

(i) The plan must be supported by a description of the rationale used, including the methods and data relied upon to develop the disaggregation zones, and a discussion of how the plan complies with the requirements of this paragraph. Such filing must provide information sufficient for interested parties to make a meaningful analysis of how the carrier derived its disaggregation plan.

(ii) The plan must be reasonably related to the cost of providing service for each disaggregation zone within each disaggregated category of support.

(iii) The plan must clearly specify the per-line level of support for each category of high-cost universal service support provided pursuant to §§ 54.301, 54.303, and/or 54.305 and/or part 36, subpart F of this chapter in each disaggregation zone.

(iv) If the plan uses a benchmark, the carrier must provide detailed information explaining what the benchmark is and how it was determined. The benchmark must be generally consistent with how the total study area level of support for each category of costs is derived to enable a competitive eligible telecommunications carrier to compare the disaggregated costs used to determine support for each cost zone.

(3) *[Deleted.]* ~~A carrier's election of this path becomes effective upon certification by the carrier to the state commission.~~
(4) *[Deleted.]* ~~A carrier shall disaggregate and target support under this path for at least four years from the date of certification to the state commission except as provided in paragraph (d)(5) of this section.~~

(5) A state commission *shall approve a plan as filed or* may require, on its own motion *or,* upon petition by an interested party, ~~or upon petition by the rural incumbent local exchange carrier,~~ modification to the *plan for* disaggregation and targeting of support. *If no eligible telecommunications carrier submits a disaggregation and targeting plan for a rural study area, the state commission shall determine the plan.* ~~selected under this path.~~

(6) *In a study area where no* ~~A~~ carrier *is* ~~not~~ subject to the jurisdiction of a state, e.g., certain tribally owned carriers, *the universal service Administrator shall establish a plan that complies with the requirements of this section.* ~~may select Path 3, but must certify to the Federal Communications Commission as described in paragraphs (d)(1) through (5) of this section.~~

(e) *Additional Procedures Governing Disaggregation and Targeting Plans*. ~~the Operation of Path 2 and Path 3:~~ *A* disaggregation and targeting plan adopted under paragraph~~s (c) or~~ (d) of this section shall be subject to the following general requirements:

(1) Support available to the ~~carrier's~~ study area under *the* ~~its~~ disaggregation plan shall equal the total support available to the study area without disaggregation.

(2) The ratio of per-line support between disaggregation zones for each disaggregated category of support shall remain fixed over time, except as changes are allowed pursuant to paragraph (c) and (d) of this section.

(3) The ratio of per-line support shall be publicly available.

(4) Per-line support amounts for each disaggregation zone shall be recalculated whenever the *study area's* ~~carrier's~~ total annual support amount changes using the changed support amount and lines at that point in time.

(5) Per-line support *to all eligible telecommunications carriers* for each category of support in each disaggregation zone shall be determined such that the ratio of support between disaggregation zones is maintained and that the product of all *eligible telecommunications* ~~of the~~ carrier's lines for each disaggregation zone multiplied by the per-line support for those zones when added together equals the sum of the *eligible telecommunications carriers'* ~~carrier's~~ total support.

~~(6) Until a competitive eligible telecommunications carrier is certified in a study area, monthly payments to the incumbent carrier will be made based on total annual amounts for its study area divided by 12.~~

~~(7) When a competitive eligible telecommunications carrier is certified in a study area, per-line amounts used to determine the competitive eligible telecommunications carrier's disaggregated support shall be based on the incumbent carrier's then-current total support levels, lines, disaggregated support relationships, and, in the case of support calculated under subpart K of this part, customer classes.~~

(f) *Submission of Information to the Administrator*:

(1) *The state commission shall submit a certification as to the plan it has approved to the universal service Administrator by a deadline to be established by the Administrator. If the state commission does not submit such a certification as to an approved plan, the Administrator shall establish a plan that complies with the requirements of this section.* ~~A carrier certifying under paragraph (b) of this section that it will not disaggregate and target high-cost universal service support shall submit to the Administrator a copy of the certification submitted to the state commission, or the Federal Communications Commission, when not subject to state jurisdiction.~~

(2) ~~A carrier electing to disaggregate and target support under paragraph (c) of this section shall submit to the Administrator a copy of the order approving the disaggregation and targeting plan submitted by the carrier to the state commission, or the Federal Communications Commission, when not subject to state jurisdiction, and a copy of the disaggregation and targeting plan approved by the state commission or the Federal Communications Commission.~~

~~(3) A carrier electing to disaggregate and target support under paragraph (d) of this section shall submit to the Administrator a copy of the self-certification plan including the information submitted to the state commission pursuant to paragraphs (d)(2)(i) and (d)(2)(iv) of this section or the Federal Communications Commission.~~

~~(4)~~ A carrier *that has proposed a plan* ~~electing~~ to disaggregate and target support under paragraph ~~(c) or~~ (d) of this section must submit *to the state commission and* to the Administrator maps which precisely identify the boundaries of the designated disaggregation zones of support within the ~~carrier's~~ study area.

Appendix C: Wireless Embedded Cost Study Issues

Introduction

A number of parties have proposed that universal service funding for CETCs should be based on the CETCs' own "actual" (presumably embedded) costs, rather than those of the ILEC. While this proposal may be superficially attractive, it raises a host of practical and legal issues. It is unclear how these issues could be resolved without imposing extremely burdensome and intrusive regulatory requirements on CETCs – requirements that would blatantly violate the Commission's established policy of eliminating such regulatory obligations for nondominant service providers such as wireless carriers. In addition, the process of developing appropriate accounting and costing standards for CETCs would be complex and contentious. The accounting and costing rules governing ILEC cost studies have evolved over the last sixty to seventy years in numerous long and hotly contested proceedings. Alltel does not believe it would be in the public interest or consistent with the deregulatory and pro-competitive framework of the Telecommunications Act for the Commission to embark on a similar path for CETCs.

Our focus here is on the practical problems that would inevitably arise if the Commission were to require wireless carriers to conduct embedded cost studies as the basis for receiving universal service funding. The basic assumption is that, under such a proposal, wireless carriers would need to develop their costs in a manner roughly parallel to the costing methods used by the ILECs to determine their high cost support from each of the principal high cost mechanisms. We first address the methodological issues that would need to be resolved to develop cost study procedures for wireless carriers. We then address the issues that would arise from the use of the existing USF rules to determine CETC support levels.

Cost Study Methodological Issues

In order to develop wireless carriers' embedded costs in a manner that at least reasonably parallels the approach used by the ILECs, the following issues would need to be addressed:

- Accounting Standards – ILECs record their costs in accordance with the accounting classifications and practices prescribed in the Uniform System of Accounts (Part 32). Wireless carriers, however, are not subject to a USOA and, as such, the accounting practices and classifications used by different wireless carriers are unlikely to be consistent. In addition, because wireless carriers' operations, revenue types and network configurations are not the same as the ILECs', their accounting classifications and practices are quite different from those of the ILECs. In order to provide a consistent cost basis for universal service support payments between ILECs and wireless carriers, the Commission would need to develop a USOA for wireless carriers that paralleled the accounting classifications and practices used by the ILECS to the greatest extent possible. Aside from imposing a significant regulatory burden on wireless carriers, this would not be a trivial task. The differences in the operations, revenue types and network configurations between wireless carriers and ILEC would make it difficult to map wireless carriers' costs and revenues into an account structure that was reasonably comparable to Part 32 (essentially a square peg-round hole problem). Also, differences in

accounting practices (e.g., capitalization versus expensing, treatment of deferred taxes, etc.) could result in wireless carriers being forced to restate their books – a potentially complex and time-consuming exercise.

- Identification of "Unregulated" Costs – The second step in developing ILEC cost studies is the identification, allocation and removal of the costs of their unregulated activities pursuant to Part 64. To mimic the distinction between regulated and unregulated costs faced by the ILECs (one that has never applied to the wireless industry), costs related to wireless carriers' "unregulated" operations would need to be identified and removed from the study. While some wireless carrier activities have obvious parallels to the unregulated activities of ILECs, others are less obvious. For example, it is unclear whether an activity such as billing incollects and outcollects, which has no precise parallel in the wireline industry, would be treated as unregulated or regulated. Also, some potentially "unregulated" activities of wireless carriers, such as provision of multi-function wireless handsets as part of various contractual service plans, may be sufficiently integrated into their operations that it would be difficult or impossible to accurately identify the associated costs.

- Separation of State and Interstate Costs – Because LSS, ICLS and LTS payments are based on ILEC interstate costs developed through the Part 36 separations process, a parallel process would need to be developed to separate wireless carriers' costs. This would likely prove to be even more difficult than developing a parallel USOA because the configuration of wireless RF networks and MTSO switching architectures simply do not correspond to the plant categories that drive much of the separation of ILEC costs. In addition, the types of traffic studies (24/7 measurement) performed by the ILECs in the past to develop traffic factors, such as the dial equipment minute (DEM) factor, are not routinely conducted by wireless carriers nor is their traffic measurement software typically configured to separately identify state and interstate traffic. Other complications, such as the lack of prescribed rates of return and depreciation rates for wireless carriers, would also need to be addressed and resolved.

- Identification of Switch and "Loop" Costs – Because HCL, ICLS and LTS are based on ILEC loop costs and LSS is based on ILEC local switching costs, identification of the comparable facilities deployed by wireless carriers will be necessary to assign costs to these two "buckets". As CMRS carriers do not have loops in the same sense that ILECs do, it is likely that some portion of the costs of CMRS carriers' radio networks (towers, cell site and switch based radio equipment, and backhaul facilities) would have to be used as a surrogate for loop costs. Because it could be maintained that not all of these costs are directly related to providing customer "access" (i.e., some are traffic sensitive as cell site capacity is routinely expanded to accommodate increased traffic volumes), some mechanism would need to be developed to separately identify the access and traffic sensitive portion of radio network costs. It's not obvious how this would be accomplished. In addition, because wireless MTSOs perform a wider range of functions than wireline switches, it is not clear whether it would be reasonable to simply use MTSO costs as a surrogate for ILEC local switching costs. If not, some not altogether obvious, but likely complex, process to disaggregate MTSO costs between a "local switching" component and an "other" component (e.g., RF network monitoring) would need to be developed.

- Disaggregation of Rural and Non-Rural Costs - This is a critical issue because those USF payments that are based on embedded costs are directed to rural ILEC study areas. These study areas have little or no relation to the (typically larger) RSA, MSA, MTA, and BTA based areas served by wireless carriers. Using actual wireless serving areas as the "study area" for determining USF costs could either:
  - Unduly favor a wireless carrier if it obtained USF for areas in which the ILEC received no USF or received USF based on the non-rural mechanisms, or
  - Unduly disadvantage a wireless carrier if its costs of serving non-rural areas were averaged with its costs of serving rural areas because it typically will incur higher costs per customer in rural ILEC service areas than it does in RBOC or other non-rural ILEC areas.

  Because wireless carriers provide service on an integrated basis throughout their service areas, any process to separately identify rural costs will inevitably be both complex and arbitrary. There is no simple and accurate way to identify wireless rural area costs (cell sites cover both rural and non-rural areas, MTSOs switch calls from both areas, maintenance costs and customer records are not separately tracked, etc.). Approximations could be made but these would be arbitrary and potentially contentious.

All of these issues would need to be addressed in order to develop embedded cost study standards for wireless carriers. Developing these standards so that they would be consistent within the wireless industry and with ILEC costing procedures would be a complex, lengthy and controversial process. Implementation of the cost study standards would be administratively burdensome and subject wireless carriers to an unprecedented and highly intrusive level of regulation. And, the results of the cost studies would, as are those of ILECs, be somewhat arbitrary and fail to reflect economic costs.

Determining USF Payments Using Wireless Embedded Costs

Although Alltel believes that the use of embedded costs are an inappropriate mechanism to determine high cost support for any provider, in order for any proposal to use embedded costs for wireless carriers to be equitable and competitively neutral, USF payments based on a wireless carrier's embedded cost study would need to be determined in a manner that parallels the approaches used by the rural ILECs as closely as possible. In this section, the basis for calculating ILEC USF support under each of the high cost mechanisms will be briefly described along with an analogous potential approach for wireless carriers. Because some of the inputs used to calculate USF support are specific to ILECs (nationwide average cost per loop, subscriber line charge revenue and DEM weighting), the application of these ILEC based standards to wireless carriers would be a somewhat contrived and convoluted process.

High Cost Loop Fund (HCL)

HCL support is determined by the amount that a carrier's annual average total (unseparated) cost per loop exceeds 115% of the nationwide average cost per loop (fixed at $240 and adjusted annually for inflation) with higher relative support the higher a carrier's loop cost. Thus, for a study area with less than 200,000 lines, a carrier receives 65% of its total loop costs

that are between 115% and 150% of the national average and 75% of its costs over 150% of the national average.

While a wireless carrier's annual total "loop surrogate" cost per customer in rural areas could be estimated from its embedded cost study (using an approximation of the methodology prescribed in Part 36.621), compared to the nationwide average cost per loop and the appropriate recovery percentages applied, the nationwide average cost per loop derived exclusively from ILEC data would no longer be an appropriate benchmark. If HCL support for CETCs were to be based on their embedded "loop surrogate" costs, it would be necessary to reinitialize the nationwide average loop cost benchmark to incorporate both wireline and wireless costs. However, this would be impossible to do without forcing all wireless carriers (not only CETCs) to conduct embedded cost studies. The absurdity of this nevertheless logical outcome further demonstrates the problems with any attempt to apply ILEC based USF standards to wireless carriers.

Local Switching Support (LSS)

For an ILEC, LSS is calculated by multiplying the difference between its weighted dial equipment minute (DEM) factor and unweighted DEM factor by its total annual local switching cost/revenue requirement (calculated pursuant to Part 54.301). The unweighted DEM factor is simply the percentage of the ILEC's switched minutes that are interstate. The DEM weighting factor employed depends on the number of lines in the ILEC's study area as follows:

NUMBER OF ACCESS LINES IN SERVICE IN STUDY AREA	WEIGHTING FACTOR
0 - 10,000	3.0
10,001 - 20,000	2.5
20,001 - 50,000	2.0
50,001 - or above	1.0

For wireless carriers, determining their LSS based on their own embedded costs would be problematic because they typically serve lines in multiple rural ILEC study areas using switches that serve more than 50,000 customers – just as many rural ILECs do (and many more probably could and should in order to maximize efficiencies).

One approach to estimating the applicable DEM weighting for a wireless carrier would be to develop a weighted average of the DEM weighting factors used by each of the rural ILECs in the wireless carrier's service area. The factor for each study area would then be weighted by the relative number of customers served by the wireless carrier in that study area to construct a composite DEM weighting factor for the rural study areas in a state. A wireless carrier's LSS would then be determined by subtracting its unweighted DEM from its composite weighted DEM and multiplying the result by its total annual switching cost/revenue requirement (paralleling the 54.301 rules to the extent possible). Again, the need to use such a complex and convoluted approach in order to parallel ILEC USF standards indicates the inappropriateness of these standards for wireless carriers.

Conclusion

While it may be theoretically possible to develop embedded cost standards for wireless carriers, the process would be difficult, lengthy and highly controversial. In order to achieve results that were consistent within the wireless industry and with ILEC standards, an unprecedented degree of intrusive and burdensome regulation would have to be imposed on wireless carriers-regulation that is inappropriate for a competitive industry. In addition, the studies would only produce estimates of embedded fully distributed costs (a widely discredited costing standard), not economic costs. And, the attempt to apply the existing ILEC centric rules to determine support payments under each USF mechanism would require reliance on benchmarks, assumptions and calculations that have little or no relevance to wireless carriers. Alltel believes it would better serve the public interest to adopt an economic cost standard for both rural ILECs and wireless carriers than attempt the Rube Goldberg-like process of adapting the existing embedded cost standards to wireless carriers.